No. 02-42

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Supreme Court, U.S.
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In The
Supreme Court of the United States

FRANCHISE TAX BOARD OF
THE STATE OF CALIFORNIA,

Petitioner,

v.

GILBERT P. HYATT AND EIGHTH JUDICIAL DISTRICT
COURT OF THE STATE OF NEVADA,

Respondents.

On Writ Of Certiorari To The
Supreme Court Of The State Of Nevada

BRIEF OF PETITIONER

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QUESTION PRESENTED

Did the Nevada Supreme Court impermissibly interfere with California's capacity to fulfill its sovereign responsibilities, in derogation of Article IV, Section 1, by refusing to give full faith and credit to California Government Code section 860.2, in a suit brought against California for the torts of invasion of privacy, outrage, abuse of process, and fraud alleged to have occurred in the course of California's administrative efforts to determine a former resident's liability for California personal income tax?

LIST OF PARTIES

Petitioner Franchise Tax Board of the State of California

Respondent Gilbert P. Hyatt

Respondent Eighth Judicial District Court of the State of Nevada, in and for the County of Clark

TABLE OF CONTENTS

	Page
Question Presented	i
List of Parties	ii
Table of Contents	iii
Table of Authorities	iv
Opinions Below	1
Jurisdiction	1
Constitutional Provisions and Statutes Involved	2
Statement of the Case	3
Summary of Argument	11
Argument	14
Conclusion	38

TABLE OF AUTHORITIES

Page

CASES:

Allstate Insurance Co. v. Hague, 449 U.S. 302 (1981) 15, 16, 26, 27, 28

Baker v. General Motors Corp., 522 U.S. 222 (1998) ... 15, 16

Bull v. United States, 295 U.S. 247 (1935) 32

California v. Grace Brethren Church, 457 U.S. 393 (1982) 32

Carroll v. Lanza, 349 U.S. 408 (1955) 15, 16, 23

Estin v. Estin, 334 U.S. 541 (1948) 23

Fair Assessment in Real Estate Ass'n v. McNary, 454 U.S. 100 (1981) 32

Franchise Tax Board v. Alcan Aluminum Ltd., 493 U.S. 331 (1990) 32

Franchise Tax Board v. United States Postal Serv., 467 U.S. 512 (1984) 31

Guarini v. New York, 521 A.2d 1362 (N.J. Super. Ct.), *aff'd*, 521 A.2d 1294 (N.J. Super. Ct. App. Div. 1986), *cert. denied*, 484 U.S. 817 (1987) 28, 29, 30

Mejia-Cabral v. Eagleton School, Inc., No. 97-2715, 1999 Mass. Super. LEXIS 353 (Mass. Super. Ct. Sept. 15, 1999) 29, 30

Milwaukee County v. M.E. White Co., 296 U.S. 268 (1935) 22

Mitchell v. Franchise Tax Board, 183 Cal.App.3d 1133, 228 Cal.Rptr. 750 (1986) 11

Nevada v. Hall, 440 U.S. 410, *reh'g denied*, 441 U.S. 917 (1979) ..... *passim*

TABLE OF AUTHORITIES – Continued

Page

Pacific-Employers Insurance Co. v. Industrial Accident Comm'n of Cal., 306 U.S. 493 (1939) 15, 16, 17, 18

Phillips Petroluem Co. v. Shutts, 472 U.S. 797 (1985) 15, 16

Sun Oil Co. v. Wortman, 486 U.S. 717 (1988) 15, 16, 23

Whittel v. Franchise Tax Board, 231 Cal.App.2d 278, 41 Cal.Rptr. 673 (1964) 9

CONSTITUTIONS:

United States Constitution, Article IV, § 1 ..... 2, 21

United States Constitution, Article IV, § 2 22

United States Constitution, Article IV, § 3 21

United States Constitution, Article IV, § 4 21

STATUTES:

28 U.S.C. § 1257(a) 1

28 U.S.C. § 1341 32

California Code of Civil Procedure § 1060.5 ..... 2, 34

California Government Code § 860.2 ..... 2, 11, 35

California Government Code § 905.2 ..... 2, 11

California Government Code § 911.2 ..... 2, 11

California Government Code § 945.4 ..... 2, 11

California Revenue & Taxation Code § 17001 ..... 2, 3

California Revenue & Taxation Code § 17014 ..... 2, 9

California Revenue & Taxation Code § 17015 ..... 2, 9

TABLE OF AUTHORITIES – Continued

Page

California Revenue & Taxation Code § 17016.....2, 9

California Revenue & Taxation Code § 19041.....2, 4, 34

California Revenue & Taxation Code § 19044.....2, 34

California Revenue & Taxation Code § 19045.....2, 34

California Revenue & Taxation Code § 19046.....2, 34

California Revenue & Taxation Code § 19047.....2, 34

California Revenue & Taxation Code § 19381.....2, 34

California Revenue & Taxation Code § 19501.....2, 3

California Revenue & Taxation Code § 19504.....2, 10

California Revenue & Taxation Code § 21021.....3, 11, 34

Title 18, California Code of Regulations § 17014 (1988).....3, 9

OTHER AUTHORITIES:

Benjamin Cardoza, *The Growth Of The Law* 136 (1924).....22

Hawaii (HAW. REV. STAT. ANN. § 662-15(2) (Michie 2002)).....12

Idaho (IDAHO CODE § 6-904A(1) (Michie 1998)).....12

James D. Sumner, Jr., *The Full-Faith-And-Credit Clause – It's History And Purpose, 34 Oregon Law Review* 224 (1955).....21

Massachusetts (MASS. GEN. LAWS ANN. ch. 258, § 10(d) (West 1988) & Supp. 2002)).....12

MINN. STAT. sections 270.275-276 (1998 & Supp. 2002) (limitations on immunity).....12

TABLE OF AUTHORITIES – Continued

Page

Minnesota (MINN. STAT. ANN. § 3, 736, subd. (3)(C) 1998 & Supp. 2002).....12

Mississippi (MISS. CODE ANN. § 11-46-9(1)(I) (2002).....12

Nebraska (NEB. REV. STAT. § 81-8, 219(2) (1996)).....12

Oklahoma (OKLA. STAT. ANN. tit. 51, § 155(11) (West 2000 & Supp. 2002)).....12

Robert H. Jackson, *Full Faith And Credit – The Lawyer's Clause Of The Constitution*, 45 Colum. L. Rev. 1 (1945).....22, 23

South Dakota (S.D. CONST. art III, § 27; S.D. CODIFIED LAWS §§ 21-32-16- to -18 (Michie 1987) §§ 3-22-10, -17) (Michie 1994)).....12

THE FEDERALIST, No. 42.....24

Utah (UTAH CODE ANN. §§ 63-30-10(8), 59-1-704 (1997 & Supp. 2002)).....12

Vermont (V.T. STAT. ANN. tit. 12, § 5601(e)(2) (1973 & Supp. 2001)).....12

OPINIONS BELOW

The written decision of the Nevada Supreme Court in Docket Numbers 35549 and 36390, dated April 4, 2002 (Order Granting Petition for Rehearing, Vacating Previous Order, Granting Petition for a Writ of Mandamus in Part in Docket No. 36390, and Granting Petition for Writ of Prohibition in Part in Docket No. 35549). Pet.App. at pp. 5-18.

The written decision of the Nevada Supreme Court in Docket Numbers 35549 and 36390, dated June 13, 2001, (Order Granting Petition (Docket No. 36390) and Dismissing Petition (Docket No. 35549)). Pet.App. at pp. 38-44.

The written decision of the Nevada Supreme Court in Docket Numbers 39274 and 39312, dated April 4, 2002 (Order Denying Petition for a Writ of Mandamus or Prohibition and Dismissing Appeal), pertaining to the Protective Order. Pet.App. at pp. 19-21.

The Protective Order of the Eighth District Court of the State of Nevada. Pet.App. at pp. 22-35.

JURISDICTION

On April 4, 2002, the Nevada Supreme Court issued its orders (1) denying and granting in part Petitioner's Petitions for Writ of Mandamus and Writ of Prohibition, and (2) denying Petitioner's Petition for Writ of Mandamus and Writ of Prohibition pertaining to the protective order. On July 2, 2002, Petitioner filed a petition for a writ of certiorari. Certiorari was granted on October 15, 2002. The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(a).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

(Set forth verbatim in Appendix, *infra*, App. 1)

United States Constitution, Article IV, § 1

California Code of Civil Procedure § 1060.5

California Government Code § 860.2

California Government Code § 905.2

California Government Code § 911.2

California Government Code § 945.4

California Revenue & Taxation Code § 17001

California Revenue & Taxation Code § 17014

California Revenue & Taxation Code § 17015

California Revenue & Taxation Code § 17016

California Revenue & Taxation Code § 19041

California Revenue & Taxation Code § 19044

California Revenue & Taxation Code § 19045

California Revenue & Taxation Code § 19046

California Revenue & Taxation Code § 19047

California Revenue & Taxation Code § 19381

California Revenue & Taxation Code § 19501

California Revenue & Taxation Code § 19504

California Revenue & Taxation Code § 21021

Title 18, California Code of Regulations § 17014

STATEMENT OF THE CASE

1. Summary of the Background

Pursuant to its inherent sovereign power, the State of California imposes a personal income tax upon the income of its residents. The Petitioner is the Franchise Tax Board of the State of California (hereinafter referred to as the "FTB"). The FTB is the California state agency charged with the public duty of implementing and enforcing California's Personal Income Tax Law. Cal. Rev. & Tax. Code §§ 17001 and 19501. Respondent Gilbert P. Hyatt is a former long-time resident of the State of California who filed a return for 1991 with the FTB asserting that he terminated his California residency and moved to Nevada on October 1, 1991, just before certain companies paid him $40 million cash in "patent licensing fees" for patents he obtained while a resident of California. Record of Proceedings at Volume 1, Item 1, p. 3 and Gilbert Hyatt's First Amended Complaint, Pet.App. at p. 78, ¶60.

Hyatt did not report the $40 million as California income subject to the state personal income tax. Record of Proceedings at Volume 3, Item 2, pp. 12-33. The FTB conducted an audit investigation of Hyatt's filing status and issued Notices of Proposed Assessment for the years 1991 and 1992 based upon its determination that Hyatt remained a California resident until April 3, 1992. Record of Proceedings at Volume 3, Item 2, pp. 412-416. In these Notices of Proposed Assessment the FTB also asserted a

civil fraud penalty. Hyatt filed a protest[1] of these Notices of Proposed Assessment. That protest is still pending in California. Record of Proceedings at Volume 3, Item 2, pp. 410-411. After filing his protest, Hyatt filed a suit against the FTB in Nevada seeking a declaration that he was a Nevada resident, a non-resident of California, and is, therefore, not subject to California personal income tax. In the Nevada suit, Hyatt also seeks monetary damages against the FTB for alleged fraud, abuse of process, invasion of privacy, outrage and negligence by the FTB and its agents both in California and Nevada. Complaint JA at pp. 45-70, and Amended Complaint Pet.App. at pp. 49-90.

Hyatt's declaratory relief action was dismissed on the FTB's motion for judgment on the pleadings for lack of subject matter jurisdiction. Order Granting Partial Motion for Judgment on the Pleadings, JA at pp. 93-95. But the trial court refused to dismiss the remaining damage claims. Instead, the Nevada District Court sealed the courtroom from public access. JA at pp. 87-92. The Nevada District Court also imposed a Protective Order upon the FTB preventing it from providing most – if not all – of the information it had obtained in the lawsuit to the FTB officials who were conducting the ongoing administrative tax protest. The order barred the FTB from providing any such documents that Hyatt had designated as confidential, without his permission. The Protective Order requires that, if Hyatt refuses permission, the FTB protest officials must attempt to obtain the documents through California

[1] A "protest" triggers an internal administrative review of the proposed assessments conducted by a hearing officer who is an employee of the FTB. Cal. Rev. & Tax Code § 19041.

judicial processes. Pet.App. at pp. 22-35. In addition, the Nevada District Court ordered the FTB to produce certain documents that, under California evidentiary and administrative laws, would not be required to be disclosed. JA at pp. 135-146.

On December 27, 1999, the Nevada District Court adopted its Discovery Commissioner's Report and Recommendation, which expanded the scope of Hyatt's lawsuit beyond torts that were allegedly committed in Nevada by California government officials into a general inquiry of every aspect of the California tax process as it applied to Hyatt:

> 4. [T]hat the entire process of the FTB audits of Hyatt, including the FTB assessments of taxes and the protests, is at issue in this case and a proper subject of discovery. . . . Hyatt's claim of fraud against the FTB entitles him to discovery on the entire audit and assessment process performed by the FTB that was and is directed at him as part of the FTB's attempt to collect taxes from Hyatt.
>
> 5. [T]he process of the FTB audits directed at Hyatt is squarely at issue in this case.

JA at pp. 137-138.

In explanation of his findings, the Discovery Commissioner explained:

> COMMISSIONER BIGGAR: " . . . but the process I think is still fair game, and if you think otherwise you will have to have the judge say that because obviously in my view if we are only concerned with acts that took place in the state

> of Nevada, then we would have a very small range of discovery in this case because I think everybody is in agreement there were only some few certain acts done in Nevada, investigation by the FTB on premises, so to speak, here as well as inquiring with various Nevada companies and other things, but in my view is only a part of the process of collecting the tax from Mr. Hyatt, and ***the process is what is under attack here***, and I think in my view, particularly a state agency should feel that its process should be open to exploration in a case such as this so that we have an open form of government."

JA at p. 133. Emphasis added.

Findings 4 and 5 of the Nevada Court made the entire audit in California, Nevada, or elsewhere the subject of litigation to determine if government power was improperly used to assess taxes and a fraud penalty. The scope of discovery allowed permits Hyatt to discover and litigate in the Nevada courts every aspect of the governmental functions of California's tax audit. This includes reviewing all decisions made to determine if California's administration of its taxing powers was improper and whether its assessment of a fraud penalty was made for the purpose of allegedly "extorting" a settlement.

The FTB filed its first petition with the Nevada Supreme Court in Docket Number 35549, contesting these discovery orders and the protective order. Record of Proceedings at Volume 1, Item 1.

While that first writ was pending before the Nevada Supreme Court, the FTB filed a motion in the trial court seeking summary judgment on the remaining tort claims and dismissal of the action for lack of jurisdiction. Franchise

Tax Board of the State of California's Motion for Summary Judgment Under Nevada Rules of Civil Procedure, Section 56(b) Or Alternatively For Dismissal Under Nevada Rules of Civil Procedure, Section 12(h)(3). Record of Proceedings at Volume 2, Item 11, Exhibit 7. That motion was denied by the district court, and the FTB filed a second petition in the Nevada Supreme Court, Docket Number 36390. Record of Proceedings at Volume 2, Item 10.

On June 13, 2001, the Nevada Supreme Court granted the FTB's second petition, finding that Hyatt had failed to show any evidence of tortious conduct on the part of the Franchise Tax Board:

> There is no evidence, aside from Hyatt's own conclusory allegations, that the Franchise Tax Board's investigation unreasonably intruded into his private life or seclusion, published false information about him, or published information to third parties that was not of a legitimate public concern. The myriad depositions and documents submitted to this court are undisputed and indicate that Franchise Tax Board's investigative acts were in line with a standard investigation to determine residency status for taxation pursuant to its statutory authority.

Pet.App. at pp. 42-43. The Court ordered the trial court to enter summary judgment in favor of the FTB and dismissed the FTB's first petition as being moot. Pet.App. at pp. 43-44.

On July 5, 2001, Hyatt filed a petition for rehearing. Real Party in Interest Gilbert P. Hyatt's Petition for Rehearing re the Court's June 13, 2001 order. JA at pp. 246-297.

On April 4, 2002, the Nevada Supreme Court, without setting forth any new evidence, vacated its earlier decision and issued a new one denying the FTB's petitions. Pet.App. at p. 5. Returning the matter to the trial court, the Nevada Supreme Court refused to apply California law immunizing the FTB from liability for the alleged common-law intentional torts, stating its justification as follows:

> We believe that greater weight is to be accorded Nevada's interest in protecting its citizens from injurious intentional torts and bad faith acts committed by sister states' government employees, than California's policy favoring complete immunity for its taxation agency.

Pet.App. at pp. 12-13. (Footnote omitted.)

Except for one document, the court also ordered the disclosure and release of the FTB's privileged documents. And the court refused to disturb the "protective order."[2] Pet.App. at p. 22.

2. The Underlying FTB Audit Investigation

The State of California imposes a personal income tax upon the income of its residents. California residents include: (1) every individual who is in California for other than a temporary or transitory purpose; and (2) every individual domiciled in California who is outside California for a temporary or transitory purpose. Cal. Rev. & Tax.

[2] The order also dismissed the the FTB's appeal from the same order.

Code §§ 17014, 17015, 17016. The purpose of these statutes is to ensure that all those who are in California for other than a temporary or transitory purpose, and enjoying the benefits and protection of the State, should in return contribute to the support of the State.[3] When a California taxpayer claims to have changed his or her state of residence, the FTB sometimes performs a residency audit to determine whether the individual did, in fact, become a non-resident of California on or near the asserted change of residency date shown on the taxpayer's California tax return. The residency audit attempts to verify when the taxpayer established significant permanent ties with the new State of claimed residency, and whether the taxpayer severed significant permanent ties with California on or near the asserted change of residency date.

In 1990, Hyatt obtained a patent on certain computer technologies, resulting in over one hundred million dollars of income in late 1991 and 1992. Substantial publicity surrounded Hyatt's patent, including a newspaper article that attracted an FTB auditor's attention in 1993. The 1992 article reported that Hyatt lived in Las Vegas, but was involved in a California legal dispute with his ex-wife about earnings from recent patent awards. Record of Proceedings at Volume 3, Item 11, pp. 53-91.

The FTB initiated an audit of Hyatt's 1991 tax return. Record of Proceedings at Volume 3, Item 11, Exhibit 7, p. 53. In accordance with the provisions of California's

[3] Cal. Code Regs. tit. 18, § 17014 (1988); *Whittel v. Franchise Tax Board*, 231 Cal.App.2d 278, 285, 41 Cal.Rptr. 673 (1964).

Personal Income Tax Law, FTB auditors attempted to obtain information and records verifying Hyatt's claim of California non-residency. JA at pp. 181-191. The FTB talked by phone to third parties with potentially relevant information, such as the Clark County Assessor's Office, and kept records reflecting the nature of each inquiry. Record of Proceedings at Volume 3, Item 11, Exhibit 2. The FTB interviewed third parties in California and Nevada, such as Hyatt's neighbors and relatives, and in some instances obtained statements from them about Hyatt's change of residency claim. Record of Proceedings at Volume 3, Item 11, Exhibit 2. The FTB also corresponded by mail with third parties either by letter alone, or by a letter accompanied by a "Demand to Furnish Information," a standard FTB form reflecting the statutory authority to obtain information in a tax audit. Cal. Rev. & Tax. Code § 19504; JA at pp. 185-188. FTB auditors also traveled to Las Vegas in March 1995, and spent partial days on each of three consecutive days visiting businesses, talking to neighbors and neighborhood workers, and observing Hyatt's alleged Nevada residence. JA at pp. 187-188.

During late November 1995, the FTB lead auditor, Sheila Cox, also accompanied another FTB auditor to Las Vegas to assist on the other auditor's cases, and made a brief observation of Hyatt's alleged residence during the trip. Hyatt claims that during this latter trip, Ms. Cox went through Hyatt's garbage, rifled through Hyatt's mail, and trespassed on Hyatt's property. JA at p. 189. The FTB disputes Hyatt's version of events on this trip. JA at pp. 181-191.

3. California's Immunity Statutes

California law provides immunity for the State, its taxing agencies, officials, and employees for injuries caused by instituting an administrative tax proceeding and for acts incidental to the assessment or collection of a tax. The immunity statute, which has no geographical restriction on its application, provides:

> Neither a public entity nor a public employee is liable for an injury caused by:
>
> (a) Instituting any judicial or administrative proceeding or action for or incidental to the assessment or collection of a tax.
>
> (b) An act or omission in the interpretation or application of any law relating to a tax.

California Government Code § 860.2.[4]

SUMMARY OF ARGUMENT

California's broad statutory scheme of immunities protects its ability to carry out its core sovereign responsibilities both within and outside of its own territorial

[4] This statute has been broadly construed by California courts. *Mitchell v. Franchise Tax Board*, 183 Cal.App.3d 1133, 1136, 228 Cal.Rptr. 750 (1986). California Government Code § 860.2 is not the only immunity statute applicable in this case: California Government Code §§ 911.2, 905.2, and 945.4 also bar money damage suits against state agencies. California statutes do not, however, provide the State with absolute immunity: for example, California Revenue and Taxation Code § 21021 establishes a cause of action in California's own courts for a tax agency's failure to follow published procedures.

borders; however, Nevada courts refused to recognize California's immunities in this lawsuit. California contends that full faith and credit requires Nevada courts to recognize California's immunities.[5]

In *Nevada v. Hall*, 440 U.S. 410, *reh'g denied*, 441 U.S. 917 (1979), addressing the facts presented by that case, this Court adhered to a generally recognized exception arising in choice-of-law cases that full faith and credit need not be extended to laws of a sister State where those laws conflict with the forum State's own policies. This exception has arisen in cases involving suits between private parties involving the question of whether the forum State or a different State's laws should apply. In footnote 24 of *Nevada v. Hall,* the Court anticipated a case such as the present one and explained that where the refusal to extend full faith and credit poses a "substantial threat to our constitutional system of cooperative federalism" (440

[5] Immunity statutes reflect a State's sovereign choice to define the limits of its exposure to liability for the action of its governmental officials, balancing principles of fairness against the legitimate needs of government. The immunities provided by California are commonly provided to tax administrators throughout the country, for example: Hawaii HAW. REV. STAT. ANN. § 662-15(2) (Michie 2002); Idaho (IDAHO CODE § 6-904A(1) (Michie 1998)); Massachusetts (MASS. GEN. LAWS ANN. ch. 258, § 10(d) (West 1988 & Supp. 2002)); Minnesota (MINN. STAT. ANN. § 3, 736, subd. (3)(C) 1998 & Supp. 2002), *but see, e.g.*, MINN. STAT. §§ 270.275-276 (1998 & Supp. 2002) (limitations on immunity)); Mississippi (MISS. CODE ANN. § 11-46-9(1)(I) (2002)); Nebraska (NEB. REV. STAT. § 81-8, 219(2) (1996)); Oklahoma (OKLA. STAT. ANN. tit. 51, § 155(11) (West 2000 & Supp. 2002)); South Dakota (S.D. CONST. art. III, § 27; S.D. CODIFIED LAWS §§ 21-32-16 to -18 (Michie 1987) §§ 3-22-10, -17) (Michie 1994)); Utah (UTAH CODE ANN. §§ 63-30-10(8), 59-1-704 (1997 & Supp. 2002)); Vermont (V.T. STAT. ANN. tit. 12, § 5601(e)(2) (1973 & Supp. 2001)).

U.S. at 424 n.24), such as where it interferes with a State's "capacity to fulfill its own sovereign responsibilities" (*ibid.*), a "different analysis or a different result" (*ibid.*) might be required. In this case a different analysis is required because the analysis under existing full faith and credit cases is inadequate to deal with the facts of this case.

California believes that this different analysis requires a different rule of law, one that is both simple and straightforward, and one which takes into consideration the concerns identified by the Court in footnote 24. California submits that:

> A forum State may not refuse to extend full faith and credit to the legislatively immunized acts of a sister State when such a refusal interferes with the sister State's capacity to fulfill its own core sovereign responsibilities.

This rule is designed to eliminate the threat to cooperative federalism by mandating full faith and credit in those circumstances where refusal to extend full faith and credit to a State's legislatively immunized acts would interfere with a State's ability to carry out its core sovereign responsibilities. This rule is supported by (1) the history of the Full Faith and Credit Clause, (2) this Court's own jurisprudence, and (3) the jurisprudence of other States interpreting and applying *Nevada v. Hall*.

In addition, when the present case is examined under the rule suggested above, it is clear that the rule applies and that Nevada courts must extend full faith and credit to California's immunity laws because (1) California's conduct of the Hyatt residency tax audit is a core sovereign responsibility, and (2) Nevada's refusal to extend full

faith and credit to California's immunity statutes *interferes* with California's capacity to conduct the Hyatt residency tax audit. When these two requirements of the rule are met, Nevada must extend full faith and credit because its refusal to do so poses a "substantial threat to our constitutional system of cooperative federalism." *Ibid.*

ARGUMENT

I. THE NEVADA SUPREME COURT VIOLATED ARTICLE IV, SECTION 1 OF THE CONSTITUTION BY REFUSING TO RECOGNIZE CALIFORNIA'S IMMUNITY STATUTES IN A LAWSUIT AGAINST THE STATE OF CALIFORNIA BY A PRIVATE CITIZEN THAT AROSE OUT OF ACTIVITIES INCIDENTAL TO THE ASSESSMENT AND COLLECTION OF CALIFORNIA STATE TAXES

A. The Current Choice-of-Law Analysis Does Not Adequately Resolve the Constitutional Issues in the Present Case; a New Rule is Needed

California's dispute with Nevada's courts presents a constitutional confrontation that goes to the very core of cooperative federalism and raises important constitutional questions that existing cases do not adequately answer. California believes that these unanswered questions require this court to adopt a new rule, a rule that California submits is necessary to resolve the "substantial threat to our constitutional system of cooperative federalism" (*Nevada v. Hall*, 440 U.S. at 424 n.24) that is presented by this case. The new rule is, in fact, suggested by the

language in footnote 24 of this Court's opinion in *Nevada v. Hall*.

Under this new rule, Nevada (or any forum State) may not refuse to extend full faith and credit to the legislatively immunized acts of a sister State when such a refusal interferes with the sister State's capacity to fulfill its own core sovereign responsibilities. This rule necessarily limits the ability of a forum State to use its own law to extend its judicial authority beyond its own geographic borders to interfere with the governmental policies and actions of a sister State.

The existing choice-of-law rules are inadequate to address a case such as this where the subject of the litigation is the manner in which a sister State is conducting a core government function. In general, this Court has explained that as long as a forum State has sufficient contacts with a lawsuit, it is not required to use the law of a sister State when to do so would offend its own public policy. *See Baker v. General Motors Corp.*, 522 U.S. 222, 232-33 (1998); *Sun Oil Co. v. Wortman*, 486 U.S. 717, 733 (1988); *Phillips Petroluem Co. v. Shutts*, 472 U.S. 797, 818-19 (1985); *Carroll v. Lanza*, 349 U.S. 408, 412 (1955); *Pacific-Employers Insurance Co. v. Industrial Accident Comm'n of Cal.*, 306 U.S. 493, 501-505 (1939) (hereinafter referred to as *Pacific Insurance*); *Allstate Insurance Co. v. Hague*, 449 U.S. 302, 308 (1981).

However, these cases are inadequate to address the constitutional issue framed by footnote 24 in *Nevada v. Hall* because they do not involve the exercise of core government activities. They fail to address the constitutional issues because they focus on the forum State's interest as a forum and the interest of the party filing suit,

rather than on the effect the choice of law will have on the non-forum party State's ability to carry out its core functions. *Baker v. General Motors Corp.*, 522 U.S. 222, 232-33 (1998), involved a personal injury lawsuit between private parties. *Sun Oil Co. v. Wortman*, 486 U.S. 717, 733 (1988), and *Phillips Petroluem Co. v. Shutts*, 472 U.S. 797, 818-19 (1985), concerned private class actions over oil royalties. *Carroll v. Lanza*, 349 U.S. 408, 412 (1955), and *Pacific-Employers Insurance Co. v. Industrial Accident Commission of California*, 306 U.S. 493, 501-505 (1939), considered the issue of workmen's compensation. *Allstate Insurance Co. v. Hague*, 449 U.S. 302, 308 (1981), involved a wrongful death dispute between private parties.

In *Pacific Insurance,* the question was whether full faith and credit required California to apply Massachusetts' workers' compensation law in a case where a Massachusetts employee of a Massachusetts employer was injured in California while acting in the scope of his employment. This Court held that California was *not* required by full faith and credit to apply Massachusetts law because it contravened the policy of California's more liberal workmen's compensation Act. 306 U.S. at 502-503. *Pacific Insurance* acknowledged that Massachusetts "ha[d] an interest in safeguarding the compensation of Massachusetts employees while temporarily abroad in the course of their employment," (*ibid.*) but explained that California had a more significant interest in being able to exercise its own "constitutional authority . . . to legislate for the bodily safety and economic protection of employees injured within it." *Ibid.* In fact, this Court explained that "[f]ew matters could be deemed more appropriately the concern of the state in which the injury occurs or more completely within its power." *Ibid.* In contrast to the analysis of the

respective interests of the States, the case did not analyze the effect the choice of law would have on the non-forum State's ability to carry out its core government functions.

Nevada v. Hall posed a question similar to that in *Pacific Insurance*: does full faith and credit require California to apply Nevada law in a case which arose out of a traffic accident caused by a Nevada state employee driving in California while on Nevada state business? This Court held that California was *not* required by full faith and credit to apply Nevada's damage limitation because it contravened the policy of California's more liberal damages law. This Court examined California's interest and compared it to California's interest in *Pacific Insurance*, noting that "[a] similar conclusion is appropriate in this case." 440 U.S. at 424.

> The interest of California afforded such respect in the *Pacific Insurance* case was in providing for "the bodily safety and economic protection of employees injured within it." In this case, California's interest is the closely related and equally substantial one of providing "full protection to those who are injured on its highways through the negligence of both residents and nonresidents." To effectuate this interest, California has provided by statute for jurisdiction in its courts over residents and nonresidents alike to allow those injured on its highways through the negligence of others to secure full compensation for their injuries in the California courts.

Ibid. (citations omitted). Just as with *Pacific Insurance*, *Nevada v. Hall* analyzed the respective States' interests, but failed to analyze the effect the choice of law would have on the non-forum State's ability to carry out its core government functions.

Indeed, anticipation of this very failing appears to have prompted the concerns that were expressed in footnote 24 of *Nevada v. Hall*. Footnote 24 explained that a different analysis and different result may be necessary where a forum State's refusal to extend full faith and credit poses a substantial threat to our constitutional system of cooperative federalism.

> California's exercise of jurisdiction in this case poses no substantial threat to our constitutional system of cooperative federalism. Suits involving traffic accidents occurring outside of Nevada could hardly interfere with Nevada's capacity to fulfill its own sovereign responsibilities. We have no occasion, in this case, to consider whether different state policies, either of California or Nevada, might require a different analysis or a different result.

Id. at 424 n.24. This text illustrates that in some situations it may be necessary to develop a rule based upon effect, rather than interest. This is shown by the language "interfere with Nevada's capacity to fulfill its own sovereign responsibilities," (*ibid.*) which focuses on the effect, rather than the interest. The key is that effect must be factored in whenever the choice-of-law decision "interferes" with a State's ability to carry out its core government functions.

Both *Nevada v. Hall* and *Pacific Insurance* support our constitutional system of cooperative federalism because they allow a State to apply its own law in cases where full faith and credit would otherwise force application of a foreign law contrary to its own policy. Both are "interest" based cases that focus primarily on the forum States' *interest* in applying their own law: in *Pacific Insurance*, California's interest in applying its own workmen's

compensation law to an employee injured while on the job in California; and in *Nevada v. Hall*, California's interest in applying its own more liberal damages law. In these cases, cooperative federalism was served by an interest-based analysis, but application of only the interest-based analysis in this case actually *thwarts* cooperative federalism because it fails to consider the effect the choice of law would have on the non-forum State's ability to carry out its core government functions. This failure to factor in the effect on core government functions is why a new rule or test must be developed.

When the *subject* of the litigation is the State's *activities* in carrying out its critical or core governmental functions, the ordinary rules are inadequate because they do not provide any consideration for effect on the State's *ability* to carry out its essential functions. Under the interest test, any law reflecting conflicting policy of the forum State, no matter how insignificant, will trump the non-forum State's law, no matter how adversely it affects its ability to carry out vital governmental functions.

In some cases, such as this one, it is the use of the interest-based test, alone, that creates a threat to cooperative federalism because it completely fails to examine whether the choice-of-law decision has the effect of interfering with the non-forum State's ability to carry out its core sovereign functions. In order to remedy this threat to cooperative federalism, California has developed what it believes is the best test that can be used where the litigation involves legislatively immunized activities undertaken in carrying out the State's core government functions, a test that looks to the *effect* of the choice-of-law decision, *i.e.*, whether there is interference. Specifically, the California rule provides that:

> A forum State may not refuse to extend full faith and credit to the legislatively immunized acts of a sister State when such a refusal interferes with the sister State's capacity to fulfill its own core sovereign responsibilities.

In addition to resolving the threat to cooperative federalism posed by using only the interest-based test, California's proffered rule should be adopted because it is supported by the history of the Full Faith and Credit Clause, this Court's own jurisprudence, and the jurisprudence of various other States in interpreting and applying *Nevada v. Hall*.

1. The History of the Full Faith and Credit Clause Supports California's Suggested Rule

Prior to the adoption of the Articles of Confederation and the Constitution, each state (or colony) was a sovereign and independent government. As independent governments they had the power to enact laws governing local matters, wage war, levy taxes and engage in any number of acts of sovereign responsibility. As independent nations they were free to accept or reject the laws or acts of other nations subject only to treaties or principles of comity. Prior to the Articles of Confederation, the colonies had to a large extent ignored the rulings of other colonies and even some of the rulings of England. Litigants could re-litigate their cases in different jurisdictions without much concern for rulings in other colonies. However, more enlightened principles of comity (at least regarding judgments) took

hold before the enactment of the Articles of Confederation.[6] These principles of comity, which were based upon enlightened self-interest, and which meant that most colonies granted full credit to other State's judgments and court rulings, were then incorporated into the Articles of Confederation.[7]

At the Constitutional Convention of 1787, these principles were explicitly included in Article IV, Section 1 of the United States Constitution; indeed, they were expanded to include in addition each State's public acts and records. The Full Faith and Credit Clause of the United States Constitution specifically provides that:

> Full faith and credit shall be given in each state to the public Acts, Records, and judicial Proceedings of every other State. And the Congress may by general Laws prescribe the Manner in which such Acts, Records and Proceedings shall be proved, and the Effect thereof.

U.S. Const., art. IV, § 1.

The Full Faith and Credit Clause was placed in Article IV along with other provisions designed to establish a single republic with equal privileges being accorded the several States,[8] and the citizens of each state throughout the rest of

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[6] James D. Sumner, Jr., *The Full-Faith-And-Credit Clause – It's History And Purpose*, 34 Or. L. Rev. 224, 228-229 (1955).

[7] *Ibid.*

[8] Article IV, § 3, Clauses 1 and 2 deal with new States, while Article IV, § 4 guarantees every State a republican form of government and protects each State from invasion and domestic violence.

the United States.[9] It establishes the importance of single nationhood, with the promise that the obligations and privileges of the States and their citizens would not end at one State's border.

Despite the dearth of legislative history, there is little doubt that the Full Faith and Credit Clause was intended to ensure harmony and peaceful intercourse among the states without relying on the uncertainties of comity.[10] It was, in effect, an internal treaty among the States. As such, although the several States maintained all the sovereignty not ceded to the nation, they also collectively forged a single integrated union where, unlike foreign nations, the States were not free to ignore the laws and acts of the nation or their sister States, even when those laws might conflict with their own:

> [T]he very purpose of the full faith and credit clause was to alter the status of the several states as independent foreign sovereigns, each free to ignore obligations created under the laws or by judicial proceedings of the others, and to make them integral parts of a single nation. . . .

Milwaukee County v. M.E. White Co., 296 U.S. 268, 276-77 (1935).

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[9] Article IV, § 2, Clause 1 provides that "citizens of each state shall be entitled to all privileges and immunities of citizens in the several states[;]" and § 2, Clause 2 provides that fugitives from justice from one state shall "be removed [back] to the state having jurisdiction of the crime."

[10] Robert H. Jackson, *Full Faith And Credit – The Lawyer's Clause Of The Constitution*, 45 Colum. L. Rev. 1, 5 n.17 (1945); Benjamin Cardoza, *The Growth Of The Law* 136 (1924).

The purpose of full faith and credit was, then, to alter the status of the States, which it did by abandoning reliance on comity and making conflict of law principles constitutionally mandated. The Full Faith and Credit Clause "substituted a command for the earlier principles of comity and *thus* basically altered the status of the States as independent sovereigns." *Estin v. Estin*, 334 U.S. 541, 546 (1948) (emphasis added). Indeed, "the clause . . . made conflicts principles enforceable as a matter of constitutional command rather than leaving the enforcement to the vagaries of the forum's view of comity." *Sun Oil Co. v. Wortman*, 486 U.S. at 723, n.1.

Years ago this Court recognized that the Clause would be properly invoked to restrain "any policy of hostility to the public Acts [of another state]." *Carroll v. Lanza*, 349 U.S. 408, 413 (1955). In this case, Nevada's refusal to extend full faith and credit to California's immunity laws results in a "policy of hostility" to California's tax acts, a policy that the Full Faith and Credit Clause was intended to restrain. This restraint against hostility can be accomplished by this Court adopting California's suggested rule.

While there may be little legislative history on the Full Faith and Credit Clause,[11] this Court's historical analysis supports California's interpretation that full faith and credit provides a virtual absolute barrier to one State allowing its processes – including its courts – to impinge upon the constitutionally valid exercise of a sister State's sovereign responsibilities. This interpretation is based on

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[11] *See Nevada v. Hall*, 440 U.S. 410; Jackson, *supra* note 10, at 5 n.17.

the principles of cooperative federalism and reciprocal respect, which are at the heart of the Full Faith and Credit Clause. It is likely that Nevada's refusal to extend full faith and credit in this case is just what the Full Faith and Credit Clause was designed to thwart.[12]

2 The Fact That This Court's Own Jurisprudence Recognizes the Limitations of an Interest-Based Test Supports the Rule California Suggests

The rule that California advances here – that a forum state may not refuse to extend full faith and credit to the legislatively immunized acts of a sister State when such a refusal interferes with the sister State's capacity to fulfill its own core sovereign responsibilities – is grounded in the concerns expressed by the Court in footnote 24 of *Nevada v. Hall*, 440 U.S. 410. *Nevada v. Hall* was a tort action against the State of Nevada in a California state court, which arose out of a traffic accident caused by a Nevada state employee driving in California while on Nevada state business. This Court held that a court need not give full faith and credit to another State's laws if those laws conflicted with the *policy* of the forum State; thus, California need not give full faith and credit to Nevada's statutory

[12] In THE FEDERALIST, No. 42, James Madison noted that the clause was "an evident and valuable improvement on the clause relating to this subject in the articles of Confederation" and that the power "may be rendered a very convenient instrument of justice, and be particularly beneficial on the borders of contiguous States, where the effects liable to justice may be suddenly and secretly translated in any stage of the process, within a foreign jurisdiction." THE FEDERALIST No. 42 (James Madison).

limitation on liability for injuries caused by a Nevada state employee since it was in conflict with California's policy against any such limitation. This holding was tied to the Court's own interest-based choice-of-laws analysis adopted in cases involving lawsuits between two private litigants. However, footnote 24 in *Nevada v. Hall* makes it clear that ruling itself was fact-based and limited; it acknowledges that a different analysis and different result may be necessary where a forum State's refusal to extend full faith and credit poses a "substantial threat to our constitutional system of cooperative federalism." *Id.* at 424 n.24.

The thrust of footnote 24 is that this different analysis and result is necessary to protect "our constitutional system of cooperative federalism." *Ibid.* Nevada's refusal to extend full faith and credit to California's immunity laws in this case poses the very threat to the constitutional system of cooperative federalism that footnote 24 cautions against. Footnote 24 suggests that it is improper to deny full faith and credit where to do so "interfere[s] with [the sister State's] capacity to fulfill its own sovereign responsibilities." *Ibid.* While a suit involving a traffic accident occurring outside of Nevada could hardly interfere with Nevada's capacity to fulfill its own sovereign responsibilities, a suit against California based on activities such as the Hyatt residency audit, which is incident to the assessment or collection of a California state tax, clearly "interferes" with California's "capacity to fulfill its own sovereign responsibilities." *Ibid.* California submits that the concerns articulated in footnote 24 can best be addressed by California's effects-based test: a forum State may not refuse to extend full faith and credit to the legislatively immunized acts of a sister State when such a

refusal interferes with the sister State's capacity to fulfill its own core sovereign responsibilities.

Footnote 24 does not exist in a vacuum; Justice Blackmun's dissent in *Nevada v. Hall* places it in perspective. Justice Blackmun warns against almost precisely what has occurred in this situation. ("States probably will decide to modify their tax-collection and revenue systems in order to avoid the collection of judgments." *Id.* at 429.) Footnote 24's cautionary instructions have appeared in other decisions of this Court, as well. For example: Justice Stevens, the author of the majority opinion in *Nevada v. Hall,* authored a concurring opinion in *Allstate Insurance Co. v. Hague*, 449 U.S. 302 (1980),[13] that is consistent with California's suggested rule. Justice Stevens recognized

[13] In *Allstate*, a Wisconsin resident employed in Minnesota died on his way to work in Minnesota when the motorcycle he was on was struck from behind by an automobile while he was still in Wisconsin. The operators of both vehicles were Wisconsin residents, neither of who had valid insurance. The decedent had a policy covering three vehicles he owned with uninsured motorist coverage for $15,000 for each vehicle. *Id.* at 305. The widow moved to Minnesota for reasons unrelated to the litigation and filed suit in Minnesota, where she sought declaratory relief under Minnesota law that the three policies could be "stacked." The defendant claimed that Wisconsin law, which precluded such "stacking," should apply. *Ibid.* The plurality opinion of this Court concluded that full faith and credit did not require Minnesota to apply Wisconsin law because, even though application of Minnesota law may have been unsound as a matter of conflict of laws, there was no threat to Wisconsin's sovereignty by allowing the use of Minnesota's substantive law. *Id.* at 313. The plurality opinion further concluded that due process did not prevent Minnesota from applying its own law since neither the "stacking" rule itself nor Minnesota's application of it to the private litigants raised any serious question of fairness. *Id.* at 320.

that full faith and credit mandates that States not infringe on other State's sovereignty:

> The Full Faith and Credit Clause implements this design by directing that a State, when acting as a forum for litigation having multistate aspects or implications, respect the legitimate interests of other States and avoid infringement upon their sovereignty.

Id. at 322 (Stevens, J., concurring). While "respect [for] the legitimate interests of other States" (*ibid.*) acknowledges the need for an interest-based test in some circumstances, Justice Stevens' recognition that States must "avoid infringement upon [other State's] sovereignty," (*ibid.*) suggests the need for an effect-based test that focuses on interference or "infringement upon . . . sovereignty." *Ibid.* Justice Stevens also explained that:

> The kind of state action the Full Faith and Credit Clause was designed to prevent has been described in a variety of ways by this Court. In *Carroll v. Lanza*, 349 U.S. 408, 413 (1955), the Court indicated that the Clause would be invoked to restrain "any policy of hostility to the public Acts" of another State. In *Nevaaa v. Hall*, *supra*, at 424, n. 24, we approved action which "pose[d] no substantial threat to our constitutional system of cooperative federalism." And in *Thomas v. Washington Gas Light Co.*, U.S. 261, 272 (1980), the plurality opinion described the purpose of the Full Faith and Credit Clause as the prevention of "parochial entrenchment on the interests of other States."

Id. at 323 n.10 (Stevens, J., concurring). These concerns are addressed in the present case by an effect-based rule. For example: his statement that *Nevada v. Hall* posed "no

substantial threat to our constitutional system of cooperative federalism," *ibid.* is especially significant because it suggests that in a proper case – such as this case – where there is such a threat, the Full Faith and Credit Clause would bar the forum State from using its own law when doing so would create – as here – a "substantial threat to our constitutional system of cooperative federalism." *Ibid.* California's effect-based test accomplishes this. In addition, California's suggested rule is the very least that is necessary to guard against the evils Justice Stevens identified in *Allstate*, and specifically to "restrain 'any policy of hostility to the public Acts' of another State," and to prevent the "parochial entrenchment on the interests of other States." *Ibid.*

3. The Jurisprudence of Other State's Interpreting And Applying *Nevada v. Hall* Supports California's Suggested Rule

The courts of other States have also recognized (as footnote 24 suggests) that *Nevada v. Hall's* interest-based test is inadequate and does not apply where the case deals with a forum State's interference with a sister State's ability to carry out its core sovereign responsibilities. These cases fully support the rule California advances: that a forum State may not refuse to extend full faith and credit to the legislatively immunized acts of a sister State when such a refusal interferes with the sister State's capacity to fulfill its own core sovereign responsibilities. These cases recognize that the failure to extend full faith and credit under such circumstances has an adverse effect on principles of cooperative federalism.

In *Guarini v. New York*, 521 A.2d 1362 (N.J. Super. Ct.), *aff'd*, 521 A.2d 1294, 1366-67 (N.J. Super. Ct. App. Div. 1986), *cert. denied*, 484 U.S. 817 (1987), New Jersey claimed that the Statue of Liberty and the island on which it is located were under its jurisdiction and sovereignty. New York had exercised jurisdiction over the statue and the island for at least 150 years. New Jersey sued the State of New York in a New Jersey court, but the New Jersey court dismissed the case in reliance on footnote 24 of *Nevada v. Hall*. *Guarini* held that the "ruling [in *Nevada v. Hall*] did not mean that a state could be sued in another state as a matter of course." *Id.* at 1366. The court dismissed the action based on the threat it posed to the constitutional system of cooperative federalism, including a potential "cascade of lawsuits" by one State's citizens against neighboring States:

> The present case clearly requires a "different analysis" and a "different result." . . . Plaintiff if successful, would clearly interfere with New York's capacity to fulfill its own sovereign responsibility over those two islands in accordance with and as granted by the 1833 compact. Exercise of jurisdiction by this court would thereby pose a "substantial threat to our constitutional system of cooperative federalism."

Ibid.

In *Mejia-Cabral v. Eagleton School, Inc.*, No. 97-2715, 1999 Mass. Super. LEXIS 353 (Mass. Super. Ct. Sept. 15, 1999), plaintiff sued a Massachusetts school in a Massachusetts state court for wrongful death caused by a juvenile delinquent attendee. The State of Connecticut was joined as a third-party defendant under the theory that it negligently placed the juvenile at the school. The Massachusetts court dismissed the State of Connecticut as a defendant, noting that:

> The prospect of one state's court deciding whether another state was negligent in selecting a particular rehabilitation program for a juvenile offender is profoundly troubling, and this court's assertion of jurisdiction over such a claim against the State of Connecticut would pose a "substantial threat to our constitutional system of cooperative federalism." The State of Connecticut makes a compelling argument that this third-party complaint would, if allowed to proceed, "interfere with [Connecticut's] capacity to fulfill its own sovereign obligations" and that recognition of its sovereign immunity is therefore mandatory.

Id. at *6 (citations omitted).

Both *Mejia-Cabral* and *Guarini* acknowledged the lawsuits against Connecticut and New York, respectively, interfered with those States' ability to carry out their sovereign functions. The Massachusetts court in *Mejia-Cabral* acknowledged that allowing the third-party complaint to proceed against the State of Connecticut would "interfere with [Connecticut's] capacity to fulfill its own sovereign obligations." *Ibid.* Similarly, the New Jersey court in *Guarini* acknowledged that if the plaintiff prevailed in the lawsuit, that result "would clearly interfere with New York's capacity to fulfill its own sovereign responsibility." *Guarini*, 521 A.2d at 1366-67.

Both courts also recognized that it was this *interference* with a State's capacity to fulfill its *sovereign responsibilities* that posed the substantial threat to constitutionally-based cooperative federalism. Finally, both courts concluded that these threats to cooperative federalism were unacceptable; they clearly recognized the need to remedy threats to our constitutional system of cooperative federalism. A similar threat to cooperative federalism

exists in the present case; it is this threat that is the justification for the effect-based rule that California asks this Court to adopt.

B. The Nevada State Court Is Required to Extend Full Faith and Credit to California's Immunity Statutes in This Case Because Its Refusal to Do So Would Interfere with California's Capacity to Fulfill its Own Core Sovereign Responsibilities

California has established above that full faith and credit requires the adoption of the rule that a forum State may not refuse to extend full faith and credit to the legislatively immunized acts of a sister State when such a refusal interferes with the sister State's capacity to fulfill its own core sovereign responsibilities. When this case is examined under the rule, it is clear that Nevada courts must extend full faith and credit to California's immunity laws because (1) California's conduct of the Hyatt residency tax audit is a *core sovereign responsibility*, and (2) Nevada's refusal to extend full faith and credit to California's immunity statutes *interfered* with California's capacity to fulfill its core sovereign responsibilities.

1. California's Rule Applies in This Case Because the FTB's Conduct of the Hyatt Residency Tax Audit Is a Core Sovereign Responsibility

The power to tax is the most essential sovereign power of a state because it is the means by which government is able to function. Exercise of this power is unquestionably a core sovereign responsibility. "'[T]axes are the life-blood of government.'" *Franchise Tax Board v. United*

States Postal Serv., 467 U.S. 512, 523 (1984) (quoting *Bull v. United States*, 295 U.S. 247, 259 (1935)). This Court has recognized "'the imperative need of a State to administer its own fiscal operations'" and that little is "'so important a local concern as the collection of taxes.'" *Franchise Tax Board v. Alcan Aluminum Ltd.*, 493 U.S. 331, 338 (1990). Although there is no clear definition of what constitutes a core sovereign responsibility, the cases cited above underscore the vital nature of the collection of state taxes, and the administration of state tax laws. Indeed, it is fair to say that California's income tax laws and its laws for the administration of income taxes are fundamental to its fiscal integrity. It is difficult, in fact, to imagine a more core sovereign responsibility than the administration of a tax system and the collection of taxes thereunder.

The notion that state taxes are too important to the States to be interfered with by outside influences is further underscored by the fact that Congress has enacted the Tax Injunction Act (28 U.S.C. § 1341), which recognizes that the autonomy and fiscal stability of the States survive best when state tax systems are not subject to scrutiny in federal courts. *Fair Assessment in Real Estate Ass'n v. McNary*, 454 U.S. 100, 102-03 (1981).[14]

The determination of residency is a foundational step in the collection of state personal income taxes. Here, all of the FTB's acts were performed as a part of the determination of

[14] For example: *California v. Grace Brethren Church*, 457 U.S. 393, 408-11 (1982), recognized the importance of tax administration to local government when it upheld the dismissal of a plaintiff's action pursuant to the Tax Injunction Act on the grounds, *inter alia*, that tax collection constitutes an important local concern of the State.

residency, and thus were undertaken as part of the State of California's inherent sovereign responsibility and power to assess and collect taxes. The process used by California is typical and reasonable given the nature of Hyatt's residency claims.[15] Any reasonable long-time California resident who claims to move to Nevada at virtually the instant he realizes $40 million in income should expect that California would use the normal procedures at its disposal to ascertain the validity of the alleged change of residence.

No State can effectively carry out its tax administration functions without being able to freely review and investigate taxpayer's claims, even when they involve a claimed change of residency. Where the claimed events allegedly take place outside of the State, effective review and investigation necessarily involves some out-of-state review; however, the out-of-state investigation and review is also a core sovereign function. Here, California would have neglected its sovereign responsibility had it not undertaken some investigation in Nevada of Hyatt's alleged new residence. Full faith and credit must require the Nevada courts to apply California's governmental immunity laws regarding tax administration and collection to the entirety of the FTB's conduct, including its conduct in Nevada.[16]

[15] The Nevada Supreme Court originally found that "the myriad of depositions and documents submitted to the court are undisputed and indicate that Franchise Tax Board's investigative acts were in line with a standard to determine residency status for taxation pursuant to its statutory authority." Pet.App. at pp. 42-43.

[16] It is worth repeating that the conduct in Nevada was minimal. The FTB auditor only made two short trips to Nevada and sent correspondence from California to third parties in Nevada in an

(Continued on following page)

2. California's Rule Applies in This Case Because Nevada Interfered with California's Capacity to Conduct the Hyatt Residency Tax Audit

It is clear that Nevada's refusal to extend full faith and credit to California's tax immunity statutes interfered with California's ability to carry out its core sovereign responsibility to assess and collect taxes. California has a comprehensive tax system that balances revenue collection with taxpayer protections: on the one side it protects taxpayers by (1) permitting administrative review of tax assessments[17], (2) establishing a taxpayer's cause of action for a tax agency's failure to follow published procedures[18], and (3) allowing *de novo* judicial review of administrative tax determinations upon payment of the tax.[19] On the other side, however, it provides protection to the State, its agencies, officials and employees by providing specified

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attempt to verify the truth of Hyatt's claims regarding his alleged relocation to Nevada. This contact in Nevada is insignificant in comparison to the hundreds of hours of audit time expended in California. JA at pp. 236-237. In fact, the Nevada court noted that ninety-seven percent of the conduct complained about occurred *outside* the forum State of Nevada. JA at pp. 236-237.

[17] Hyatt still has a full slate of administrative remedies available to him including: a complete review of the tax assessment at the protest stage (Cal. Rev. & Tax. Code §§ 19041, 19044); and, an independent administrative review by the five-member State Board of Equalization (Cal. Rev. & Tax. Code §§ 19045-47).

[18] Cal. Rev. & Tax. Code § 21021.

[19] In fact, when the issue is residency – as it is here – once a taxpayer exhausts his administrative review, he is entitled to file a lawsuit seeking declaratory relief as to his residence *without* the necessity of prepaying the tax. Cal. Rev. & Tax. Code § 19381; Cal. Civ. Proc. Code § 1060.5.

immunities in connection with the administration of the tax system and the collection of taxes. This tax system reflects the California legislature's best efforts to achieve the proper balance.

The general effect of Nevada's refusal to give full faith and credit to California's immunities is to skew the tax system; thus, Hyatt retains all the benefits provided under California law, but Nevada has relieved him of the burdens. The effect of this is to *interfere* with California's capacity to assess and collect taxes. In addition, Nevada's refusal to extend full faith and credit has deprived California of reasonable reliance on an immunity statute that specifically protects its ability to enforce state tax laws.

More specifically, Nevada's refusal to give full faith and credit to California's immunities will interfere with the FTB's residency audit program, the conduct of which is a core sovereign responsibility. As part of the residency audit of Hyatt, the FTB disclosed minimal identifying information about him to others in order to determine his residency under California law. J.A. at pp. 181-191. Hyatt claims he was injured by these disclosures; however, California is immune from liability for these injuries under California Government Code § 860.2. By refusing to extend full faith and credit, Nevada has exposed the FTB's residency audit processes to both the additional legal expenses from protracted, out-of-state tort litigation, as well as potentially unlimited damages. This exposure to unlimited liability will necessarily have a chilling effect upon residency audits, which often require consulting third party sources and making minimal information disclosures out of state. Thus, by refusing to extend full faith and credit, the Nevada courts have interfered with the FTB's entire residency audit program.

Furthermore, the Nevada courts have directly, and knowingly, interjected themselves into California's administrative process. The Discovery Commissioner held variously that:

1. "[T]he entire process of the FTB audits of Hyatt, including the FTB assessments of taxes and the protests, is at issue in the case and a proper subject of discovery. . . . " JA at p. 133.

2. "[T]he process of FTB audits directed at Hyatt is squarely at issue in this case." JA at p. 133.

3. "[T]he process . . . is fair game . . . and if you think otherwise you will have to have the judge say that. . . . [T]he process is what is under attack here. . . . " JA at p. 133.

The protective order, issued by the trial court, and left in place by the Nevada Supreme Court (Pet.App. at pp. 22-35), blocks normal access to information relevant to the underlying tax assessments by denying material produced in this litigation to the California administrative process. The Nevada court's protective order dictates the mechanics of how California can use its own statutory power to obtain information in a tax audit by requiring a notice and demand procedure not contained in California law. California's normal practice of reviewing tax matters, which requires the exhaustion of administrative remedies, has been effectively bypassed. The ruling of the Nevada Supreme Court rejects California's recognized claims of privilege, including the attorney-client privilege, and

interposes Nevada's interpretation of such privileges. JA at pp. 135-146. And none of these intrusions include the toll on FTB employees and resources.[20]

Finally, if extrapolated, it is clear that the widespread application of the rule set down by the Nevada Supreme Court could (and perhaps would) interfere with (and likely cripple) the States' ability to conduct any number of various programs that are vital to state interests, each of which is a core sovereign responsibility. In order to ensure that this does not occur, and to protect the balance inherent in our Constitution's system of cooperative federalism, it is important that this Court affirm that full faith and credit applies in this case.

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[20] The Nevada District Court allowed the deposition of 24 witnesses, mostly FTB employees who were not involved at all with the Hyatt audit. These depositions totaled 315 hours of testimony and 11,000 pages of transcripts, and included 340 demands for documents made of deposed witnesses, and 5 separate voluminous written document demands which included 329 individual document demands, for which the FTB produced 17,514 pages of documents. Record of Proceedings at Volume 3, Item 11, Exhibit 8, pp. 420-422.

CONCLUSION

Based on the foregoing reasons, Petitioner respectfully requests that this Court reverse the April 4, 2002 order of the Nevada Supreme Court and order that this case be dismissed and the protective order vacated.

Respectfully submitted,

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United States Constitution

Article IV

Section 1. Full Faith and Credit shall be given in each State to the public Acts, Records, and judicial Proceedings of every other State. And the Congress may by general Laws prescribe the Manner in which such Acts, Records and Proceedings shall be proved and the Effect thereof.

California Code of Civil Procedure

§ 1060.5. Action by one claiming to be nonresident for income tax purposes

Any individual claiming to be a nonresident of the State of California for the purposes of the Personal Income Tax Law may commence an action in the Superior Court in the County of Sacramento, or in the County of Los Angeles, or in the City and County of San Francisco, against the Franchise Tax Board to determine the fact of his or her residence in this state under the conditions and circumstances set forth in Section 19381 of the Revenue and Taxation Code.

California Government Code

§ 860.2. Injuries caused by proceedings or application of laws

Neither a public entity nor a public employee is liable for an injury caused by:

(a) Instituting any judicial or administrative proceeding or action for or incidental to the assessment or collection of a tax.

(b) An act or omission in the interpretation or application of any law relating to a tax.

California Government Code

§ 905.2. Claims for money or damages against state

There shall be presented in accordance with Chapter 1 (commencing with Section 900) and Chapter 2 (commencing with Section 910) of this part all claims for money or damages against the state:

(a) For which no appropriation has been made or for which no fund is available but the settlement of which has been provided for by statute or constitutional provision.

(b) For which the appropriation made or fund designated is exhausted.

(c) For money or damages (1) on express contract, or (2) for an injury for which the state is liable.

(d) For which settlement is not otherwise provided for by statute or constitutional provision.

California Government Code

§ 911.2. Time of presentation of claims; limitation

A claim relating to a cause of action for death or for injury to person or to personal property or growing crops shall be presented as provided in Article 2 (commencing with Section 915) of this chapter not later than six months after the accrual of the cause of action. A claim relating to any other cause of action shall be presented as provided in Article 2 (commencing with Section 915) of this chapter

not later than one year after the accrual of the cause of action.

California Government Code

§ 945.4. Necessity of written claim acted upon by board or deemed to have been rejected

Except as provided in Sections 946.4 and 946.6, no suit for money or damages may be brought against a public entity on a cause of action for which a claim is required to be presented in accordance with Chapter 1 (commencing with Section 900) and Chapter 2 (commencing with Section 910) of Part 3 of this division until a written claim therefor has been presented to the public entity and has been acted upon by the board, or has been deemed to have been rejected by the board, in accordance with Chapters 1 and 2 of Part 3 of this division.

California Revenue & Taxation Code

§ 17001. Short title

This part is known and may be cited as the "Personal Income Tax Law."

California Revenue & Taxation Code

§ 17014. Resident

(a) "Resident" includes:

(1) Every individual who is in this state for other than a temporary or transitory purpose.

(2) Every individual domiciled in this state who is outside the state for a temporary or transitory purpose.

(b) Any individual (and spouse) who is domiciled in this state shall be considered outside this state for a temporary or transitory purpose while that individual:

(1) Holds an elective office of the government of the United States, or

(2) Is employed on the staff of an elective officer in the legislative branch of the government of the United States as described in paragraph (1), or

(3) Holds an appointive office in the executive branch of the government of the United States (other than the armed forces of the United States or career appointees in the United States Foreign Service) if the appointment to that office was by the President of the United States and subject to confirmation by the Senate of the United States and whose tenure of office is at the pleasure of the President of the United States.

(c) Any individual who is a resident of this state continues to be a resident even though temporarily absent from the state.

(d) For any taxable year beginning on or after January 1, 1994, any individual domiciled in this state who is absent from the state for an uninterrupted period of at least 546 consecutive days under an employment-related contract shall be considered outside this state for other than a temporary or transitory purpose.

(1) For purposes of this subdivision, returns to this state, totaling in the aggregate not more than 45 days during a taxable year, shall be disregarded.

(2) This subdivision shall not apply to any individual, including any spouse described in paragraph (3), who

has income from stocks, bonds, notes, or other intangible personal property in excess of two hundred thousand dollars ($200,000) in any taxable year in which the employment-related contract is in effect. In the case of an individual who is married, this paragraph shall be applied to the income of each spouse separately.

(3) Any spouse who is absent from the state for an uninterrupted period of at least 546 consecutive days to accompany a spouse who, under this subdivision, is considered outside this state for other than a temporary or transitory purpose shall, for purposes of this subdivision, also be considered outside this state for other than a temporary or transitory purpose.

(4) This subdivision shall not apply to any individual if the principal purpose of the individual's absence from this state is to avoid any tax imposed by this part.

California Revenue & Taxation Code

§ 17015. Nonresident

"Nonresident" means every individual other than a resident.

California Revenue & Taxation Code

§ 17016. Presumption of residence; rebuttal

Every individual who spends in the aggregate more than nine months of the taxable year within this State shall be presumed to be a resident. The presumption may be overcome by satisfactory evidence that the individual is in the State for a temporary or transitory purpose.

California Revenue & Taxation Code

§ 19041. Protest against proposed deficiency assessment; time; contents

(a) Within 60 days after the mailing of each notice of proposed deficiency assessment the taxpayer may file with the Franchise Tax Board a written protest against the proposed deficiency assessment, specifying in the protest the grounds upon which it is based.

(b) Any protest filed with the Franchise Tax Board on or before the last date specified for filing that protest by the Franchise Tax Board in the notice of proposed deficiency assessment (according to Section 19034) shall be treated as timely filed.

(c) The amendments made by the act adding this subdivision [FN1] shall apply to any notice mailed after December 31, 1999.

California Revenue & Taxation Code

§ 19044. Protest; reconsideration of assessment; hearing

(a) If a protest is filed, the Franchise Tax Board shall reconsider the assessment of the deficiency and, if the taxpayer has so requested in his or her protest, shall grant the taxpayer or his or her authorized representatives an oral hearing. Chapter 4.5 (commencing with Section 11400) of Part 1 of Division 3 of Title 2 of the Government Code does not apply to a hearing under this subdivision.

(b) The Franchise Tax Board may act on the protest in whole or in part. In the event the Franchise Tax Board acts on the protest in part only, the remaining part of the

protest shall continue to be under protest until the Franchise Tax Board acts on that part.

California Revenue & Taxation Code

§ 19045. Protest; finality of action; time for appeal

(a) The Franchise Tax Board's action upon the protest, whether in whole or in part, is final upon the expiration of 30 days from the date when it mails notice of its action to the taxpayer, unless within that 30-day period the taxpayer appeals in writing from the action of the Franchise Tax Board to the board.

(b)(1) The Franchise Tax Board's notice of action upon protest shall include the date determined by the Franchise Tax Board as the last day on which the taxpayer may file an appeal with the board.

(2) Any appeal to the board filed by the taxpayer on or before the date for filing an appeal specified in the notice (pursuant to paragraph (1)) shall be treated as timely filed.

(c) This section shall apply to any notice mailed after December 31, 1999.

California Revenue & Taxation Code

§ 19046. Appeal to Board of Equalization; addressing and mailing

Two copies of the appeal and two copies of any supporting documents shall be addressed and mailed to the State Board of Equalization at Sacramento, California. Upon receipt of the appeal, the board shall provide one copy of the appeal and one copy of any supporting

documents to the Franchise Tax Board at Sacramento, California.

California Revenue & Taxation Code

§ 19047. Appeal; hearing and determination; notice

The board shall hear and determine the appeal and thereafter shall forthwith notify the taxpayer and the Franchise Tax Board of its determination and the reasons therefor.

California Revenue & Taxation Code

§ 19381. Equitable process against assessment or collection; action to determine residence; stay of tax based upon residence

No injunction or writ of mandate or other legal or equitable process shall issue in any suit, action, or proceeding in any court against this state or against any officer of this state to prevent or enjoin the assessment or collection of any tax under this part; provided, however, that any individual after protesting a notice or notices of deficiency assessment issued because of his or her alleged residence in this state and after appealing from the action of the Franchise Tax Board to the State Board of Equalization, may within 60 days after the action of the State Board of Equalization becomes final commence an action, on the grounds set forth in his or her protest, in the Superior Court of the County of Sacramento, in the County of Los Angeles or in the City and County of San Francisco against the Franchise Tax Board to determine the fact of his or her residence in this state during the year or years set forth in the notice or notices of deficiency assessment. No tax based solely upon the residence of such

an individual shall be collected from that individual until 60 days after the action of the State Board of Equalization becomes final and, if he or she commences an action pursuant to this section, during the pendency of the action, other than by way of or under the jeopardy assessment provisions of this part.

California Revenue & Taxation Code

§ 19501. Administration and enforcement; creation of districts; branch offices

The Franchise Tax Board shall administer and enforce Part 10 (commencing with Section 17001), Part 10.7 (commencing with Section 21001), Part 11 (commencing with Section 23001), and this part. For this purpose, it may divide the state into a reasonable number of districts, in each of which a branch office or offices may be maintained during all or part of the time as may be necessary.

California Revenue & Taxation Code

§ 19504. Examination of books and papers; oral examination of taxpayer and witnesses; subpoenas

(a) The Franchise Tax Board, for the purpose of administering its duties under this part, including ascertaining the correctness of any return; making a return where none has been made; determining or collecting the liability of any person in respect of any liability imposed by Part 10 (commencing with Section 17001), Part 11 (commencing with Section 23001), or this part (or the liability at law or in equity of any transferee in respect of that liability); shall have the power to require by demand, that an entity of any kind including, but not limited to, employers, persons, or financial institutions provide

information or make available for examination or copying at a specified time and place, or both, any book, papers, or other data which may be relevant to that purpose. Any demand to a financial institution shall comply with the California Right to Financial Privacy Act set forth in Chapter 20 (commencing with Section 7460) of Division 7 of Title 1 of the Government Code. Information which may be required upon demand includes, but is not limited to, any of the following:

(1) Addresses and telephone numbers of persons designated by the Franchise Tax Board.

(2) Information contained on Federal Form W-2 (Wage and Tax Statement), Federal Form W-4 (Employee's Withholding Allowance Certificate), or State Form DE-4 (Employee's Withholding Allowance Certificate).

(b) The Franchise Tax Board may require the attendance of the taxpayer or of any other person having knowledge in the premises and may take testimony and require material proof for its information and administer oaths to carry out this part.

(c) The Franchise Tax Board may issue subpoenas or subpoenas duces tecum, which subpoenas must be signed by any member of the Franchise Tax Board and may be served on any person for any purpose.

(d) Obedience to subpoenas or subpoenas duces tecum issued in accordance with this section may be enforced by application to the superior court as set forth in Article 2 (commencing with Section 11180) of Chapter 2 of Part 1 of Division 3 of Title 2 of the Government Code.

(e) When examining a return, the Franchise Tax Board shall not use financial status or economic reality

examination techniques to determine the existence of unreported income of any taxpayer unless the Franchise Tax Board has a reasonable indication that there is a likelihood of unreported income.

(f) The amendments made by the act adding this subdivision shall apply to any examination beginning on or after the effective date of this act.

California Revenue & Taxation Code

§ 21021. Action by taxpayer aggrieved by action or omission by officer or employee in reckless disregard of published procedures; amount of damages; frivolous position; penalty

(a) If any officer or employee of the board recklessly disregards board published procedures, a taxpayer aggrieved by that action or omission may bring an action for damages against the State of California in superior court.

(b) In any action brought under subdivision (a), upon a finding of liability on the part of the State of California, the state shall be liable to the plaintiff in an amount equal to the sum of all of the following:

(1) Actual and direct monetary damages sustained by the plaintiff as a result of the actions or omissions.

(2) Reasonable litigation costs, as defined for purposes of Sections 19420 and 26491. [FN1]

(c) In the awarding of damages under subdivision (b), the court shall take into consideration the negligence or omissions, if any, on the part of the plaintiff which contributed to the damages.

(d) Whenever it appears to the court that the taxpayer's position in the proceedings brought under subdivision (a) is frivolous, the court may impose a penalty against the plaintiff in an amount not to exceed ten thousand dollars ($10,000). A penalty so imposed shall be paid upon notice and demand from the board and shall be collected as a tax imposed under Part 10 (commencing with Section 17001) or Part 11 (commencing with Section 23001).

Title 18 California Code of Regulations § 17014 (1988)

Who Are Residents and Nonresidents.

The term "resident," as defined in the law, includes (1) every individual who is in the State for other than a temporary or transitory purpose, and (2) every individual who is domiciled in the State who is outside the State for a temporary or transitory purpose. All other individuals are nonresidents.

Under this definition, an individual may be a resident although not domiciled in this State, and, conversely, may be domiciled in this State without being a resident. The purpose of this definition is to include in the category of individuals who are taxable upon their entire net income, regardless of whether derived from sources within or without the State, all individuals who are physically present in this State enjoying the benefit and protection of its laws and government, except individuals who are here temporarily, and to exclude from this category all individuals who, although domiciled in this State, are outside this State for other than temporary or transitory purposes, and, hence, do not obtain the benefits accorded by the laws and Government of this State.

If an individual acquires the status of a resident by virtue of being physically present in the State for other than temporary or transitory purposes, he remains a resident even though temporarily absent from the State. If, however, he leaves the State for other than temporary or transitory purposes, he thereupon ceases to be a resident.

If an individual is domiciled in this State, he remains a resident unless he is outside of this State for other than temporary or transitory purposes.